

## Internal Revenue Service

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Department of the Treasury  
Washington, DC 20224

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PLR-134052-07

Date:

January 17, 2008

In Re:

Legend:

Trustor =  
Trust

Date 1 =  
Date 2 =  
Date 3 =  
Date 4 =  
Brother =  
Brother's Spouse =  
Taxpayer =  
Spouse =  
Child 1 =  
Child 2 =  
Child 3 =

Child 5 =

Dear :

This is in response to the ruling request submitted by your authorized representative dated July 23, 2007, requesting estate tax and generation-skipping transfer tax rulings regarding the proposed exercise of a power of appointment.

The facts submitted indicate that Trustor died on Date 1, prior to September 25, 1985. During her lifetime, Trustor created Trust, an irrevocable inter vivos trust on Date 2. Upon creation of Trust, the trust corpus was divided into equal shares, Trust A and Trust B. Under the terms of Trust A, the entire net income is to be paid to Taxpayer during his lifetime. After Taxpayer's death, the trust income is to be paid to Spouse, if living, during her lifetime. Under subparagraph A.2 of Article 6, if such income payments are not sufficient, then the trustee is to pay to Taxpayer out of principal such sums as Taxpayer in his discretion "shall deem necessary for his proper support, care, health, and maintenance." In addition, under subparagraph A.3 of Article 6, Taxpayer has the noncumulative right to withdraw annually from trust corpus, such amounts as he requests, up to the greater of \$5,000 or 5 percent of the value of the Trust A principal. (Spouse also possessed, during the lifetime of Trustor, a noncumulative right to withdraw trust principal in an amount not exceeding \$3,000 annually.) After the death of Taxpayer, up to \$20,000 per year of Trust A principal may be distributed to Spouse for Spouse's proper support, care, health and maintenance.

In addition, under subparagraph A.6 of Article 6, Taxpayer, during his lifetime, by written instrument or by his last will and testament, has the power to appoint the Trust A corpus, "on such terms and conditions, either outright or in trust," to one or more of the class consisting of his spouse and issue.

Finally, under subparagraph A.7 of Article 6, on the death of the survivor of Taxpayer and Spouse, to the extent Taxpayer has not exercised his power of appointment, the trustee is to divide the remaining Trust A corpus into as many equal shares as there are living children of Taxpayer, and then deceased children leaving issue then surviving. The corpus of each share is to be distributed outright to the living children (all having attained the age of 35). Any share held for the living issue of a deceased child is to be held in further trust until the youngest of such issue attains age 21, at which time the corpus will be distributed outright to the issue. Under subparagraph E of Article 6, unless sooner terminated under other provisions, each trust created under the Trust instrument must terminate twenty-one years after the death of the last survivor of Trustor, Spouse, Brother, Brother's Spouse, and their issue living on Date 2.

Trust B also provided for the entire net income to be paid to Taxpayer during his lifetime, and thereafter to Spouse for her lifetime. However, during Trustor's life, and after her death, Brother and Brother's Spouse had annual noncumulative rights to withdraw trust corpus. The amount either could withdraw never exceeded the greater of 5,000 or 5% of the Trust B corpus. In addition, Brother had a power to appoint during his life by written instrument or by will any part of the principal of Trust B to or among his

spouse, his issue and Taxpayer's Spouse and issue. Under the terms of the Trust instrument, if Brother did not exercise his power, then following the deaths of Brother and Brother's Spouse, the Trust B corpus was to be distributed to Trust A and administered under the terms of Trust A. Brother died on Date 3, prior to September 25, 1985, without having exercised his power. Accordingly, under the terms of the trust instrument, following the deaths of Brother and Brother's Spouse, the Trust B corpus was distributed to Trust A and administered under the terms of Trust A. Brother's Spouse died on Date 4, after September 25, 1985.

Taxpayer is currently serving as trustee of Trust A. If Taxpayer ceases to serve as trustee, then Spouse is designated as successor trustee. Taxpayer and Spouse have 5 children, Child 1, Child 2, Child 3, Child 4 and Child 5, all of whom were living on Date 2.

Taxpayer proposes to execute a written instrument whereby he exercises the power of appointment granted under subparagraph A.6 of Article 6. The proposed exercise will be binding and irrevocable upon his death, and will become effective on the death of the survivor of Taxpayer and Spouse, except with regard to a provision (discussed below) controlling any trust corpus included in Taxpayer's gross estate, that will become effective on Taxpayer's death.

Under the proposed exercise, to the extent any portion of Trust A is included in the Taxpayer's gross estate for federal estate tax purposes, then if Spouse survives Taxpayer, that portion of the trust is to be distributed on Taxpayer's death to a separate non-exempt trust for the benefit of Spouse. The terms of this trust are identical to those terms of Trust that apply after Taxpayer's death if Spouse survives Taxpayer, during the remaining lifetime of Spouse. If Spouse does not survive Taxpayer, or upon Spouse's subsequent death, the portion of the trust corpus is to be held in separate non-exempt trusts or distributed as separate shares under the same terms and provisions as stated below. In addition, Taxpayer appoints any portion of the trust estate with respect to which Brother's Spouse is treated as the transferor for GST tax purposes (because of the lapse at her death after September 25, 1985, of her annual withdrawal power), to be held in separate non-exempt trusts or distributed as separate shares under the same terms and provisions as stated below.

With respect to the balance of the Trust A corpus, under the proposed exercise, on the death of the survivor of Taxpayer and Spouse, a 20 percent share of the trust estate is to be distributed outright to each of Child 1, Child 2 and Child 3. If any of Child 1, Child 2 or Child 3 is then deceased, then the deceased child's share is to be held in trust for the benefit of his or her then living issue by right of representation. Any such share established for the issue of Child 1, Child 2 and Child 3 is to be distributed outright to the beneficiary on the earlier of the day before 21 years after the death of the last surviving child of Taxpayer who was living on Date 2, or when the beneficiary attains age 21. If the deceased child has no surviving issue, then the share is to pass to

the Taxpayer's and Spouse's then living issue by right of representation, subject to the terms of any trust for such issue provided for under the exercise of the power.

Finally, on the death of the survivor of Taxpayer and Spouse, a 20 percent share of the trust estate is to be held in a separate trust for each of Child 4 and Child 5. Each trust provides for the discretionary payment of income and principal during the beneficiary's life for the beneficiary's support, care, health and education. On the death of Child 4 or Child 5, as the case may be, the corpus of the trust is to be distributed pursuant to the Child's exercise of a limited power to appoint the property among Taxpayer's issue. The instrument specifically provides that this power of appointment may not be exercised in a manner that defers vesting of an interest beyond the date that is the day before 21 years after the death of the last survivor of Taxpayer and his issue that were living on Date 2.

If either Child 4 or Child 5 predeceases Taxpayer and Spouse, then the deceased child's share is to be held in trust for the benefit of his or her then living issue by right of representation. Each trust provides for the discretionary payment of income and principal during the beneficiary's life for the beneficiary's support, care, health and education. Each trust is to be distributed outright to the beneficiary on the date that is the day before 21 years after the death of the last survivor of Taxpayer and his issue that were living on Date 2, or if earlier, when the beneficiary attains age 21. If the deceased child has no surviving issue, then the share is to pass to the Taxpayer's and Spouse's then living issue by right of representation subject to the terms of any trust for such issue provided for under the exercise of the power.

It is represented that no additions, actual or constructive, have been made to Trust since September 25, 1985.

Taxpayer requests the following rulings:

1. The exercise by Taxpayer of the limited power of appointment over Trust A, as proposed, will not result in any property subject to the limited power being included in Taxpayer's gross estate under section 2041.

2. The proposed exercise of the limited power by Taxpayer will not cause Trust A, or any trusts created by the exercise of the power, to lose exempt status for generation-skipping transfer tax purposes, nor will the exercise result in a transfer of property that is subject to the generation-skipping transfer tax.

#### Ruling 1

Section 2041(a)(2) provides that the value of the gross estate shall include the value of all property with respect to which the decedent has at the time of his death a general power of appointment created after October 21, 1942, or with respect to which the decedent has at any time exercised or released such a power of appointment by a

disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under sections 2035 to 2038.

Under section 2041(a)(3) and section 20.2041-3(e)(1) of the Estate Tax Regulations, the value of the gross estate includes the value of all property to the extent of any property with respect to which the decedent by will exercises a power of appointment created after October 21, 1942, by creating another power of appointment which, under the applicable local law, can be validly exercised so as to postpone the vesting of any estate or interest in such property, or suspend the absolute ownership or power of alienation of such property, for a period ascertainable without regard to the date of the creation of the first power.

Section 2041(b)(1) defines the term "general power of appointment" as a power that is exercisable in favor of the decedent, the decedent's estate, the decedent's creditors, or the creditors of the decedent's estate. A power to consume, invade, or appropriate property for the benefit of the decedent that is limited by an ascertainable standard relating to the health, education, support, or maintenance of the decedent is not a general power of appointment.

Section 20.2041-1(c)(1) provides that a power of appointment is not a general power if by its terms it is either (a) exercisable only in favor of one or more designated persons or classes other than the decedent or his creditors, or the decedent's estate or the creditors of the holder's estate, or (b) expressly not exercisable in favor of the decedent or his creditors, or the decedent's estate, or the creditors of his estate.

Under section 20.2041-1(c)(2), a power is limited by an ascertainable standard if the extent of the holder's duty to exercise and not to exercise the power is reasonably measurable in terms of his needs for health, education, or support (or any combination of them). The words "support" and "maintenance" are synonymous and their meaning is not limited to the bare necessities of life.

Section 2041(b)(2) provides that the lapse of a power of appointment created after October 21, 1942, during the life of the individual possessing the power shall be considered a release of such power. This rule applies only to the extent that the property, which could have been appointed by exercise of such lapsed powers, exceeded in value, at the time of such lapse, the greater of \$5,000 or 5 percent of the aggregate value, at the time of such lapse, of the assets out of which, or the proceeds of which, the exercise of the lapsed powers could have been satisfied.

In the present case, Taxpayer possesses a power to appoint Trust A corpus outright or in further trust to, or for the benefit of, a class consisting of Spouse and his issue. In addition, Taxpayer has the discretionary power to distribute corpus to himself for his proper support, care, health, and maintenance.

Taxpayer's power to appoint Trust A corpus is not exercisable in favor of Taxpayer, his estate, or the creditor's of his estate. Taxpayer's discretionary power to distribute corpus to himself is limited by an ascertainable standard relating to his health, maintenance, support and education. Therefore, these powers do not constitute general powers of appointment under sections 2041(a)(2) and 2041(b)(2), and the possession of these powers will not cause Trust A to be included in Taxpayer's gross estate under section 2041. Further, Taxpayer's proposed exercise of the power to appoint Trust A corpus, as described above, will not result in the creation of other powers of appointment described in section 2041(a)(3).

Accordingly, we conclude that the exercise by Taxpayer of the limited power of appointment over Trust A, as proposed, will not result in any property subject to the limited power being included in Taxpayer's gross estate under section 2041.

However, we note that under Trust A, Taxpayer does possess, during his lifetime, the noncumulative right to withdraw annually from trust corpus, up to the greater of \$5,000 or 5 percent of the value of the Trust A principal. In accordance with section 2041(a)(2) and section 2041(b)(2), Taxpayer will possess a general power of appointment in the year of his death, with respect to the property subject to this power, assuming Taxpayer has not exercised his annual withdrawal right at the time of his death. The value of the property subject to this power at the time of Taxpayer's death will be includible in the Taxpayer's gross estate under section 2041(a)(2).

## Ruling 2

Section 2601 imposes a tax on every generation-skipping transfer (GST) made by a "transferor" to a skip person. In general, under section 2652(a)(1) and section 26.2652-1(a)(1), of the Generation-Skipping Transfer Tax Regulations, the individual with respect to whom the property was last subject to Federal estate or gift tax is the transferor of the property for GST tax purposes.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 (the Act), 1986-3(Vol. 1) C.B. 1, and section 26.2601-1(b)(1)(i) of the regulations, provide that the generation-skipping transfer tax shall not apply to any generation-skipping transfer under a trust that was irrevocable on September 25, 1985. However, this rule does not apply to the extent that such transfer was not made out of corpus added to the trust after September 25, 1985 (or out of income attributable to corpus so added). Further, the rule does not apply to a transfer of property pursuant to the exercise, release or lapse of a general power of appointment that is treated as a taxable transfer under chapter 11 or chapter 12. The transfer is made by the person holding the power at the time the exercise, release or lapse becomes effective and is not considered a transfer under a trust that was irrevocable on September 25, 1985. Section 26.2601-1(b)(1)(ii) provides that any trust in existence on September 25, 1985, will be considered irrevocable unless the settlor held a power that would have caused inclusion of the trust in the settlor's gross estate under sections 2038 or 2042 if the settlor had died on September 25, 1985.

Section 26.2601-1(b)(1)(v)(A) provides that, except as provided under section 26.2601-1(b)(1)(v)(B), where any portion of a trust remains in the trust after the post September 25, 1985, release, exercise, or lapse of a power of appointment over that portion of the trust, and the release, exercise, or lapse is treated to any extent as a taxable transfer under chapter 11 or chapter 12, the value of the entire portion of the trust subject to the power that was released, exercised, or lapsed is treated as if that portion had been withdrawn and immediately retransferred to the trust at the time of the release, exercise, or lapse. The creator of the power will be considered the transferor of the addition except to the extent that the release, exercise, or lapse of the power is treated as a taxable transfer under chapter 11 or chapter 12.

Section 26.2601-1(b)(1)(v)(B) provides a special rule for certain powers of appointment. Under this section, the release, exercise, or lapse of a power of appointment (other than a general power of appointment as defined in section 2041(b)) will not be treated as an addition to a trust if: (1) such power of appointment was created in an irrevocable trust that is not subject to chapter 13 under section 26.2601-1(b)(1); and (2) in the case of an exercise, the power of appointment is not exercised in a manner that may postpone or suspend the vesting, absolute ownership or power of alienation of an interest in property for a period, measured from the date of creation of the trust, extending beyond any life in being at the date of creation of the trust plus a period of 21 years plus, if necessary, a reasonable period of gestation (the perpetuities period). For purposes of section 26.2601-1(b)(1)(v)(B)(2), the exercise of a power of appointment that validly postpones or suspends the vesting, absolute ownership or power of alienation of an interest in property for a term of years that will not exceed 90 years (measured from the date of creation of the trust) will not be considered an exercise that postpones or suspends vesting, absolute ownership or the power of alienation beyond the perpetuities period. This section also provides that if a power is exercised by creating another power, it is deemed to be exercised to whatever extent the second power may be exercised.

In the present case, as concluded above, Taxpayer's power to appoint Trust A corpus is a limited power of appointment. The proposed exercise by Taxpayer of the limited power of appointment with respect to the portion of Trust A that is not subject to inclusion in the Taxpayer's gross estate, will not postpone or suspend the vesting, absolute ownership or power of alienation of any interest in the trust property for a period, measured from Date 2, the date of creation of the original trust, extending beyond any life in being at the date of creation of the original trust plus a period of 21 years. Nor may any limited power of appointment granted under the terms of Taxpayer's proposal be exercised in a manner that may postpone or suspend the vesting, absolute ownership or power of alienation of interests beyond any life in being on Date 2 plus a period of 21 years. Therefore, pursuant to section 26.2601-1(b)(1)(v)(B), the exercise of the power of appointment by Taxpayer, as proposed, will not be treated as an addition, constructive or otherwise, to Trust A.

Accordingly we conclude that the proposed exercise of the limited power by Taxpayer with respect to the Trust A property not subject to inclusion in the Taxpayer's gross estate, will not cause the Trust A property that is not subject to inclusion in the Taxpayer's gross estate (with the exception of the property subject to Brother's Spouse's withdrawal power discussed below), or any trusts created by the exercise of the power with respect to those assets, to lose exempt status for generation-skipping transfer tax purposes, nor will the exercise result in a transfer of property that is subject to the generation-skipping transfer tax.

However, as discussed above, Taxpayer will possess a general power of appointment in the year of his death, with respect to the property subject to his noncumulative right to withdraw annually from trust corpus, up to the greater of \$5,000 or 5 percent of the value of the Trust A principal, to the extent the power is not exercised prior to his death. The value of the property subject to this power at the time of Taxpayer's death will be includible in the Taxpayer's gross estate under section 2041(a)(2). In accordance with section 26.2601-1(b)(1)(i) and section 26.2601-1(b)(1)(v)(A), this property will not be exempt from GST tax.

Similarly, at the time of her death, Brother's Spouse possessed a general power of appointment with respect to the property subject to her right to withdraw amounts annually from the Trust B corpus, to the extent the power was not exercised prior to her death. The value of the property subject to this power at the time of Brother's Spouse's death on Date 4 after September 25, 1985 was subject to inclusion in Brother's Spouse's gross estate under section 2041(a)(2) and was distributed to Trust A after her death. In accordance with section 26.2601-1(b)(1)(i) and section 26.2601-1(b)(1)(v)(A), the portion of Trust A attributable to this property is not exempt from GST tax.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by the appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination. Except as specifically ruled above, no opinion is expressed as to the federal tax consequences of the facts described above under the cited provisions or any other provisions of the Code or regulations.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter should be attached to any gift, estate, or generation-skipping transfer tax returns that you may file relating to these matters.



In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely yours,

George Masnik  
Branch Chief, Branch 4  
Office of Associate Chief Counsel  
(Passthroughs and Special Industries)

Enclosures  
Copy for section 6110 purposes  
Copy of this letter

cc: